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No. 91-504

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In The

Supreme Court of the United States

October Term, 1991

JAMES G. SOMERVILLE, ARLENE CORBY SOMERVILLE, AND CORBY MEMORIAL TRUST,

Petitioners,

v.

NEW JERSEY,

Respondent.

Petition For A Writ Of Certiorari To The Supreme Court Of New Jersey

BRIEF AND APPENDIX IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME COURT OF NEW JERSEY

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COUNTERSTATEMENT OF THE CASE

The decedent, Harry R. Corby, was domiciled in New Jersey at the time of his death on June 23, 1983. He had previously established a trust in 1980 in which he retained the right to the use of the trust income and corpus. The trust assets were in New Jersey. Since the decedent had retained power and control over the trust income and corpus during his lifetime, the Director of the New Jersey Division of Taxation ("Director") included the trust as part of the decedent's estate subject to New Jersey transfer inheritance taxes in accordance with *N.J.S.A.* 54:34-1(c) which specifically taxes transfers "intended to take effect in possession or enjoyment at or after . . . death."

Petitioners, James G. Somerville and Arlene Corby Somerville, trustees of the trust, disagreed with the Director's determination and appealed the decision by filing a complaint in the New Jersey Tax Court, the appropriate judicial forum entrusted to adjudicate appeals from determinations of the Director. In an opinion dated November 14, 1988, Presiding Tax Court Judge Lasser addressed each of the contentions raised by Mr. and Mrs. Somerville.* Judge Lasser specifically examined the language in the declaration of trust and concluded in his opinion (set forth on page 7a of the appendix to this brief):

> It is apparent from the language of the trust that the Settlor [decedent] intended a transfer of the trust income and corpus to take effect at his

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* The petitioners failed to include the Tax Court opinion in their appendix. The Director has included the opinion in the appendix to this brief.

> death because prior to his death he had the right to take income and corpus from the trust, and this right did not terminate until his death.

Accordingly, Judge Lasser concluded that the Director correctly assessed the tax upon the trust in accordance with *N.J.S.A.* 54:34-1(c) as a transfer to take effect at death. A judgment was entered on November 18, 1988 (PCa36).

Petitioners appealed the Tax Court's determination to the Appellate Division of the New Jersey Superior Court. On November 30, 1989, in a *per curiam* decision, the Appellate Division affirmed the Tax Court's judgment for the reasons expressed in Judge Lasser's opinion (PCa33-34).

Petitioners appealed the determination of the Appellate Division to the New Jersey Supreme Court. On March 5, 1991 the New Jersey Supreme Court dismissed the appeal "for failure to state a substantial constitutional issue." (PCa5). Petitioners' motion for reconsideration was denied by the New Jersey Supreme Court on April 30, 1991 (PCa1).

ARGUMENT

SINCE THE DECEDENT RETAINED POWER AND CONTROL OVER THE TRUST INCOME AND CORPUS DURING HIS LIFETIME, SUCH TRUST PROPERTY IS SUBJECT TO THE NEW JERSEY TRANSFER INHERITANCE TAX IN ACCORDANCE WITH *N.J.S.A.* 54:34-1(c) AS A TRANSFER INTENDED TO TAKE EFFECT IN POSSESSION OR ENJOYMENT AT OR AFTER DEATH.

The authority to control, permit, regulate and condition the testate and intestate transmission and devolution of a domiciliary's property within the jurisdiction of a state resides in the state. The doctrine has been recognized in a long line of cases that such authority is part of the residue of sovereignty retained by the states, and insured by the Tenth Amendment of the Federal Constitution. *United States v. Fox*, 94 *U.S.* 315 (1877); *United States v. Perkins*, 163 *U.S.* 625 (1896); *Magoun v. Illinois Trust & Savings Bank*, 170 *U.S.* 283 (1898); *Plummer v. Coler*, 178 *U.S.* 115 (1900); *Snyder v. Bettman*, 190 *U.S.* 249 (1903); *Maxwell v. Bugbee*, 250 *U.S.* 525 (1919); *United States v. Burnison*, 339 *U.S.* 87 (1950).

The New Jersey transfer inheritance tax is a privilege levy on the right of succession to property transferred by a decedent and is levied on the transfer. *In re Estate of Anne Boyd Lichtenstein*, 52 *N.J.* 553, 247 A.2d 320 (1968). *N.J.S.A.* 54:34-1 provides that:

> . . . a tax shall be and is hereby imposed . . . upon the transfer of property, real or personal . . . or of any interest therein or income therefrom, in trust or otherwise, to or for the use of any transferee, distributee or beneficiary. . . .

> c. Where . . . property . . . is transferred by deed, grant, bargain, sale or gift . . . intended to take effect in possession or enjoyment at or after . . . death.

It is clear that in the present case the trust created by the decedent comes within the aforesaid statutory provision. The decedent retained full control over the trust as trustee and reserved the right to the use of income and principal including the right to invade the capital for his, and his family's, care and welfare and to make gifts. Moreover, the decedent reserved the power to amend the trust.

As noted by the New Jersey Supreme Court in *Darr v. Kervick*, 31 *N.J.* 476, 483-84, 158 A.2d 42 (1960):

> It is a well-established rule venerable with age, that a transfer *inter vivos* by which the donor retains a life estate in the subject matter is a transfer "intended to take effect in possession or enjoyment at or after . . . death." (citations omitted). It is substance, rather than form, which controls, and the transfer is subject to the transfer inheritance tax even if stated by its term to be absolute, if it appears that the donor in actuality retains a life interest in the property or its income. (citations omitted).

Thus the transfer of the trust property, which was located in New Jersey, upon the death of the decedent, who was domiciled in New Jersey, is clearly subject to the New Jersey tax in accordance with *N.J.S.A.* 54:34-1(c).

The petition for a writ of certiorari plainly does not present any question of constitutional dimension nor any

other basis which would warrant the granting of such relief. The petition should therefore be denied.

CONCLUSION

For the above-stated reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

Respectfully submitted,

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Dated: October 11, 1991

NOT FOR PUBLICATION WITHOUT THE APPROVAL
OF THE TAX COURT COMMITTEE ON OPINIONS

TAX COURT OF NEW JERSEY
DOCKET NO. 11-11-0315-87IT

CORBY MEMORIAL TRUST,

Plaintiff,

v.

MEMORANDUM
OPINION

STATE OF NEW JERSEY,

Defendant.

Decided November 14, 1988

James G. Somerville and Arlene Corby Somerville, *pro se*, for plaintiff.

Herbert K. Glickman for defendant (W. Cary Edwards, Attorney General of New Jersey, attorney).

LASSER, P.J.T.C.

Plaintiffs, trustees of the Corby Memorial Trust, contest a New Jersey transfer inheritance tax assessment imposed by the Director, Division of Taxation, on the transfer of assets of an *inter vivos* trust, which transfer was held by the Director to be a transfer intended to take effect at or after death, pursuant to *N.J.S.A.* 54:34-1(c). The Director moved for summary judgment on this ground and also moved to dismiss plaintiffs' complaint for failure to file in a timely manner. Plaintiffs made a cross-motion for summary judgment and, additionally, claimed that the Director failed to timely file a responsive

pleading. By consent of the parties, the matter was submitted to the court for decision without oral argument.

The Director alleges in his answer that plaintiffs failed to timely file their complaint, however, a review of the record indicates that plaintiffs timely filed within the 90-day period set forth in *N.J.S.A.* 54:51A-14 and *R.* 8:4-1(b). Correspondence from the Director to plaintiffs after they had used four days of their appeal time gave them 86 days from June 25, 1987 to appeal to the Tax Court. These 86 days expired on September 19, 1987, a Saturday. The complaint was filed on Monday, September 21, 1987. When the deadline for filing falls on a Saturday, Sunday or holiday, the time for filing is extended to the next business day. *R.* 1:3-1.

The Director was required to file his answer within 60 days, pursuant to *R.* 8:4-3. The Director timely filed his answer on November 20, 1987.

I

Harry R. Corby, as Settlor, created the Corby Memorial Trust on April 24, 1980. He died June 23, 1983. The trust agreement provided that, during his lifetime, Harry R. Corby was to serve as trustee together with his daughter, Arlene Corby Somerville, who was designated alternate trustee. Although the trust was irrevocable, Mr. Corby reserved full power and control over the trust income and reserved the right to invade corpus and amend the trust.

The trust agreement also provided that upon the death of the Settlor, Arlene Corby Somerville and her

husband, James G. Somerville, are to serve as co-trustees and the income of the trust is to be distributed as follows:

a. The net income of the trust to Arlene Corby Somerville and her husband, with the option to leave the income in the trust for accumulation;

b. $100 per month to James Corby Somerville, grandson of Harry R. Corby, with the option of contributing same back to the trust to aid its accumulation goal;

c. $100 per month for life to Nila M. Stickney, sister of Harry R. Corby, and

d. In addition to the foregoing, at the discretion of the co-trustees, donations may be made to "churches, charities, etc."

Upon the death of Arlene Corby Somerville and her husband, the net income of the trust is to be distributed to James Corby Somerville, their son, as the "anticipated final income beneficiary," for his life. The trust instrument authorizes the corpus to be invaded in the event James should suffer catastrophic illness. He also was given the option of allowing the trust income to accumulate.

Upon the death of all of the income beneficiaries, the then remaining trust corpus is to be distributed for the purposes of "charity, education, conservation, scientific and medical research."

At the time of Harry R. Corby's death, the trust corpus consisted of cash located in several New Jersey banking institutions and real property located in New Jersey. The trust instrument was signed by decedent and

notarized in New Jersey. Plaintiffs state in their complaint that the principal office of the trust is in Huntsville, Alabama, where plaintiffs reside, and they contend that the trust corpus is "domiciled" in Alabama, not in New Jersey where decedent died and where the trust corpus was physically located at the time of settlor's death.[1] Plaintiffs insist that the property belongs to a "foreign trust" over which New Jersey has no jurisdiction.

On March 14, 1985, the Transfer Inheritance Tax Bureau of the Division of Taxation notified Arlene Corby Somerville, as executrix of decedent's estate, of the assessment of a direct transfer inheritance tax due in the amount of $11,210.19, plus interest from February 23, 1984, on the transfer of trust assets which took effect upon death, and offered a compromise tax of $2,539.10 on the contingent remainder interest.[2]

Plaintiffs contend that the Director wrongfully assessed the trust, asserting the following constitutional grounds:

1. The tax is a wrongful taking of trust property by the State in violation of the United States Constitution;

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[1] Plaintiffs' statements with respect to the location of the trust appear to refer to periods after the death of the Settlor.

[2] The remainder interest is contingent because the income beneficiaries survived the decedent and have the right to invade corpus, so the value of the corpus left for the charitable remainder and the value of the contingent life estate of Settlor's grandson cannot be determined at the date of death.

2. The trust and the beneficiaries are immune from New Jersey taxes because of constitutional provisions that government cannot tax those over whom it does not govern, and

3. The trust is tax exempt since it has been granted tax exempt status under federal tax provisions, specifically § 664 of the Internal Revenue Code.

In addition, plaintiffs contend that the Director wrongfully assessed the trust assets because:

1. the Settlor intended the transfer to take effect when he created the trust, not at the time of his death;

2. the Settlor created the trust more than three years before his death; therefore, the trust was not made in contemplation of death and could not have been intended to take effect on Settlor's death;

3. the Settlor's retained rights in the trust were merely options or contingencies and, in fact, he allowed all of the income to accrue and remain in the trust, and

4. 100% of the trust property is vested in the charitable remainder trust and, therefore, the transfer of its assets are exempt from taxation by New Jersey.

The Director maintains that the trust is subject to tax under *N.J.S.A.* 54:34-1(c) as a transfer to take effect upon death because the Settlor retained full power and control over the trust income and corpus during his lifetime.

II.

Plaintiffs argue that the decedent did not intend the transfer of property to the trust to take effect upon his death and, therefore, the transfer is not subject to tax under *N.J.S.A.* 54:34-1(c). However, under the trust agreement, the Settlor, during his lifetime, retained substantial interest and control over the trust property. The agreement reserved to the Settlor "the right to use of 'net income' which may be distributed to me at my option or discretion or that of my Alternate Trustee." [Art. Second (a) (2)]

Although in the trust agreement the Settlor expressed his intention to "conserve" and "enhance" the trust's capital, he also provided that " . . . capital or corpus of this trust may be used for my care or welfare to the extent necessary or in the event of a long or catastrophic illness, or unusual circumstances such as economic failures, inflated living costs, etc. if income shall be deemed insufficient for such purposes by myself as Trustee or my Alternate Trustee acting in my behalf." Additionally, he provided that "I may continue my practice of making gifts or donations to charity, church, etc., or to members of my family from time to time from this trust. . . . " [Art. Second (b) (1) & (2)]

The trust instrument specifically provides that, at the Settlor's death, the trust income is to be distributed to the several named beneficiaries, including the plaintiffs in this case. [Art. Second (b) (1) & (2)]

Further, although accumulation of the trust corpus was a "prime and crucial objective" behind the creation

of the trust, the instrument does not command such accumulation. It states:

> Invasion of the trust corpus . . . is contrary to the philosophy and objective of the trust. However, considering realistically that circumstances of extreme need may occur, . . . the Trustee, Alternate Trustee or Successor Co-Trustee may invade capital for the care and welfare of the maker, Harry R. Corby or . . . James G. or Arlene Corby Somerville or . . . James Corby Somerville to the extent such catastrophic illness or extreme need is not covered by health insurance, veteran's benefit programs, etc. [Art. Fifth, par. 4]

It is apparent from the language of the trust that the Settlor intended a transfer of the trust income and corpus to take effect at his death because prior to his death he had the right to take income and corpus from the trust, and this right did not terminate until his death.

Plaintiffs claim that the decedent's retained rights in the trust were only options that he did not exercise during his life. However, the presence of such retained rights is sufficient to subject the transfer to tax. In *Millar v. Taxation Div. Director*, 9 *N.J. Tax* 48 (Tax Ct. 1987), the court explained that "[i]f property is transferred prior to death, it is the presence of a retained interest transferred at death which triggers taxation." 9 *N.J. Tax* at 53, citing *In re Estate of Lichtenstein*, 52 *N.J.* 553, 247 *A.*2d 320 (1968). *See also Darr v. Kervick*, 31 *N.J.* 476, 483-84 (1960); *In re Brockett's Estate*, 111 *N.J. Eq.* 183, 186 (Prerog. Ct. 1932). The court in *Millar* stated:

> . . . a transaction which comes within the statute is one in which a settlor creates a trust and transfers property to the trust but reserves the

> income to himself until his death. The settlor is not regarded as having given up the property since he retains a right to the income, which right terminates at his death, and the transfer is regarded to be effected at that time. *See Carter v. Bugbee*, 91 *N.J.L.* 438, 103 *A.* 818 (Sup. Ct. 1918), aff'd 92 *N.J.L.* 390, 160 *A.* 412 (E. & A. 1918). 9 *N.J. Tax* at 53.

The language of the trust instrument and case law support the conclusion that retention of rights by the Settlor to take income and corpus from the trust during his life, which rights do not terminate until his death, results in a transfer to the beneficiaries that takes effect on the Settlor's death, and therefore the transfer is subject to tax under *N.J.S.A.* 54:34-1(c).

Plaintiffs seek to apply the language of the "contemplation of death" presumption to the subject trust. *N.J.S.A.* 54:34-1(c) deals with two types of transfers: (1) transfers intended to take effect upon death, and (2) transfers made in contemplation of death. *N.J.S.A.* 54:34-1(c), par. 2 deems a transfer made within three years prior to death to have been made in contemplation of death. Paragraph 2 also provides that if the transfer is made prior to such three-year period, the transfer shall not be deemed to have been made in contemplation of death. Plaintiffs argue that since decedent created the trust more than three years before his death, there was no transfer intended to take effect at death.

However, the "contemplation of death" presumption has no relevance to transfers intended to take effect upon death, which are conditional transfers complete only upon the death of the transferor. The presumption relates

only to taxability of transfers made in contemplation of death, which are completed before death and are separate and distinct from transfers intended to take effect upon death.

The trust agreement also provides for a charitable remainder. At the death of the non-charitable beneficiaries, the corpus is to be used for charity, education, conservation and scientific and medical research. The taxability of the charitable remainder is not an issue in this case because the Director did not tax the charitable remainder portion of the trust. He stated in a July 14, 1986 letter to plaintiffs that the income benefits received by Arlene Corby Somerville, her husband and their son are "what has become subject to tax, and not any remaining portion that will ultimately vest in the charity involved."

Plaintiffs contend that the transfer of the assets of the trust is not taxable by the State of New Jersey because the trust is a tax-exempt charitable remainder split-interest unitrust under *I.R.C.* § 664 and therefore is exempt from New Jersey's transfer inheritance tax.

It appears that the subject trust may not comply with *I.R.C.* § 664(d)(2) because it does not provide for payment of a fixed annual percentage of at least five percent of the value of the trust assets to noncharitable beneficiaries. Additionally, the trust grants to the co-trustees and the final income beneficiary the power to invade the corpus of the trust, which appears to be contrary to the requirements of *I.R.C.* § 664(d)(2). However, the federal tax treatment of this trust has no bearing on whether the transfer of assets upon the death of the Settlor to the non-

charitable beneficiaries is taxable by the State of New Jersery [sic].

Plaintiffs also cite *I.R.C.* § 508(e) for the proposition that the trust is tax exempt. *I.R.C.* § 508(e) pertains only to provisions that must be included in the governing instrument of a private foundation in order for it to qualify for federal income tax exemption under *I.R.C.* § 501 and does not affect the taxability of the subject transfer by New Jersey.

III.

Plaintiffs assert that the State of New Jersey lacks the power or jurisdiction to tax the trust. The power to tax is conferred upon the Legislature by the *N.J. Const.* (1947) Art. VIII, § 1, par. 1.[3] In the context of the transfer inheritance tax, the New Jersey Supreme Court has affirmed the State's authority to tax such transfers. "The authority to control, permit, regulate and condition the testate and intestate transmission and devolution of a domiciliary's property within the jurisdiction of a state resides in the state." *United States v. Kingsley*, 41 *N.J.* 75 (1963). Although *Kingsley* involved a will, the language is applicable to the case at bar. The court explained the transfer inheritance tax as follows:

> In effect, the state says to a testator "You may devise or bequeath your property but in return for the privilege of doing so, a tax must be paid,

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[3] For an historical discussion of the Legislature's taxing power in general *see League of Municip. v. Kimmelman*, 105 *N.J.* 422, 428 (1987).

> the amount of which shall depend on the value of the property you devise or bequeath and on the relationship to you of the devisee or legatee you select." *Kingsley*, 41 *N.J.* at 80.

Plaintiffs further contend that the State's use of its taxing authority in this case is repugnant to the United States Constitution. However, the court in *Kingsley*, in citing several United States Supreme Court cases, stated that "[t]he doctrine has been recognized in a long line of cases that [a state's authority to regulate inheritance distribution] is part of the residue of sovereignty retained by the states, and insured by the Tenth Amendment of the Federal Constitution. [citations omitted]." *Kingsley*, 41 *N.J.* at 79. Such authority includes the legislative power to impose a tax on "the *transfer* by a resident of intangible personal property wherever situate," *Pennsylvania Co., etc. v. Kelly*, 134 *N.J.Eq.* 120, 125 (Prerog. Ct. 1943), and real property located in New Jersey. *N.J.S.A.* 54:34-1(c). *N.J.S.A.* 54:34-1 provides in relevant part:

> . . . a tax shall be and is hereby imposed . . . upon the transfer of property, real or personal, of the value of $500.00 or over, or of any interest therein or income therefrom, in trust or otherwise, to or for the use of any transferee, distributee or beneficiary . . .
>
> c. Where real or tangible personal property within this State of a resident of this State or intangible personal property wherever situate of a resident of this State . . . is transferred by deed, grant, bargain, sale or gift . . . intended to take effect in possession or enjoyment at or after such death.

The record indicates that at the date of decedent's death, funds of the trust were deposited in banking institutions within New Jersey and the trust's real property was situated within this State. The decedent was a resident of New Jersey, and there is no evidence that any of the trust assets that were real property or tangible personal property were located outside of New Jersey at the date of decedent's death. I find that the trust and its assets are subject to inheritance tax by New Jersey under *N.J.S.A.* 54:34-1.

IV

The Bureau offered a compromise tax based on its conclusion that the ultimate disposition of a portion of the taxable estate valued at $171,273.61 is contingent and taxes thereon are presently indeterminable. The Bureau calculated that the maximum contingent tax would be $17,447.32, depending on the ultimate beneficiaries and the amount received by each. The $2,539.10 compromise tax represents a present adjustment of taxes to become due in the future and is authorized by New Jersey statute. *N.J.S.A.* 54:36-6. Plaintiffs have not contested the calculation of the direct tax or the compromise tax.

I find that the Director has correctly imposed transfer inheritance tax on the transfer of assets of the Corby Memorial Trust as a transfer to take effect at death and has the constitutional and statutory authority to do so.

Director's motion for summary judgment is granted, and Director's assessment is affirmed. Plaintiffs' cross-motion for summary judgment is denied.
